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Supreme Court of the United States

OCTOBER TERM 1961.

No. 754 72

STATE OF WISCONSIN and PUBLIC SERVICE COMMISSION OF WISCONSIN, and

PUBLIC SERVICE COMMISSION OF THE STATE OF NEW YORK,
Petitioners,

v.

FEDERAL POWER COMMISSION,
Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT.

JOHN W. REYNOLDS,
Attorney General, State of Wisconsin,

ROY G. TULANE,
Assistant Attorney General, State of Wisconsin,
State Capitol,
Madison 2, Wisconsin,
Attorneys for State of Wisconsin.

WILLIAM E. TORKELSON,
Chief Counsel, Public Service Commission of Wisconsin,
State Office Building,
Madison 2, Wisconsin,
Attorney for Public Service Commission of Wisconsin.

KENT H. BROWN,
Counsel, Public Service Commission of the State of New York,
55 Elk Street,
Albany 1, New York.

BARBARA M. SUCHOW,
Assistant Counsel, Public Service Commission of the State of New York,
199 Church Street,
New York 7, N. Y.

MORTON L. SIMONS,
1815 H Street, N. W.,
Washington 6, D. C.,
Attorneys for Public Service Commission of the State of New York.

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PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT.

Petitioners, State of Wisconsin and Public Service Commission of Wisconsin, and Public Service Commission of the State of New York, pray that a writ of certiorari issue to review the judgment of the United States Court of Appeals for the District of Columbia Circuit, entered in the above-entitled case on November 30, 1961.

Opinions Below.

The opinion of the Court of Appeals (App. A, *infra*, pp. A1-A23) is not yet reported. The opinion and order of the Federal Power Commission (R. 251-342) are

reported at 24 F.P.C. 537, and the Commission's order denying rehearing (R. 395-404) is reported at 24 F.P.C. 1008. The decision of the presiding examiner (R. 35-217) is reported at 24 F.P.C. 590.

Jurisdiction.

The judgment of the Court of Appeals affirming the Commission's orders was entered on November 30, 1961 (App. B, *infra*, pp. B1-B2). The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1) and Section 19(b) of the Natural Gas Act, 15 U.S.C. 717r(b).

Question Presented.

The question is whether the Federal Power Commission, for reasons of administrative convenience, may indefinitely defer fixing just and reasonable rates for natural gas producers' sales in accordance with proven and established procedures under Sections 4 and 5 of the Natural Gas Act because it has chosen to embark upon an entirely new, unformulated and judicially untested method of producer rate regulation, when such indefinite deferral will cause massive and irreparable injury to the consuming public.

Statute Involved.

The pertinent provisions of the Natural Gas Act, 52 Stat. 821, as amended, 15 U.S.C. 717-717w, are set out in Appendix E, *infra*.

Statement.

The original proceedings, 1948-54—The Phillips Petroleum Company is a large integrated oil company, which at all times pertinent here has been and is the largest producer-seller of natural gas, accounting for approximately 10% of the national total. In October 1948, Respondent instituted an investigation under Section 5(a) of the Natural Gas Act to determine whether Phillips was a natural gas company and if so whether its rates were unjust and unreasonable (R. 17-20), 7 F.P.C. 983. Following a full-scale field investigation and hearings, Respondent in August 1951 held that Phillips was not a natural gas company, 10 F.P.C. 246. On review, the Court of Appeals for the District of Columbia Circuit reversed, and entered a judgment directing respondent to "fix the rates at which [Phillips' interstate] * * * sales are made." *Wisconsin* v. *Federal Power Commission*, 205 F. 2d 706, 712 (D.C. Cir. 1953) (R. 405-6). In June 1954, this Court affirmed the mandate of the Court of Appeals. *Phillips Petroleum Company* v. *Wisconsin*, 347 U.S. 672.

The current proceedings, 1954-62—On receipt of the Court of Appeals' mandate, Respondent reinstated its investigation into the lawfulness of Phillips' rates under Section 5(a) of the Natural Gas Act, consolidating with the investigation twelve rate increases filed by Phillips under Section 4(e) of the Act (R. 21-23).

In addition to reopening the Phillips proceeding, the Commission instituted Section 5(a) investigations into the rates of 37 producers. Eleven of these investigations, pertaining to major independent producers, have been carried forward almost to completion (App. C, *infra*, p. C1); the eleven producers account for approximately one-third of all interstate sales of natural gas. Complete cost-of-service

presentations have been introduced by the Staff in each of these cases, and hearings have been concluded in all but one. Two have already been the subject of Examiners' decisions, and in five others all briefs have been filed.[1]

The remanded hearings—The hearings on remand commenced before one of Respondent's examiners in June 1956 and concluded, after 91 days of hearing, in December 1957. During this time the record rose to 27,000 pages, with an additional 2,000 pages of exhibits and 4,000 pages of miscellaneous pleadings and orders. At the commencement of the hearing all parties agreed that Phillips' rates should be determined on a cost-of-service basis (R. 60), and Phillips cooperated in making available exhaustive data covering all phases of its natural gas business, including cost-of-service data for test years 1954 and 1956 (R. 86).

The Examiner's decision—In April 1959, the Examiner issued a 342-page decision (R. 35-217; 24 F.P.C. 590); it incorporates detailed findings as to Phillips' rate base, costs, required rate of return, and all other relevant issues, and reaches the ultimate conclusion that Phillips' jurisdictional cost of service[2] for the 1954 test year was $57.3 million, equivalent to an average unit cost of 11.7¢ per Mcf (R. 211). The Examiner directed Phillips to design and file a schedule of rates which, when applied to sales being made in 1954, would recover this cost of service. He further provided that the rates for all sales instituted after 1954 should be adjusted to conform to the schedule of rates

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[1] As petitioners point out, *infra*, pp. 16, 24-25, the record in these cases would provide a feasible and lawful basis for determining the reasonableness of current producer rate levels during the period pending completion of the area rate proceedings contemplated in Respondent's order here under review (R. 266-7).

[2] As correctly noted by the court below, "cost-of-service in this context includes not only operating expenses, taxes, exploration allowances, and gas purchases but also a fair return upon the rate base."

thus derived (R. 214). Pursuant to this direction, Phillips prepared and filed a preliminary schedule of rates (R. 218-225), but inasmuch as the Commission dismissed the proceedings, a final schedule was never submitted. (See R. 226).

The Commission's Opinion 338—Following exceptions filed by interested parties (R. 253) and oral argument, the Commission issued its Opinion No. 338 on September 28, 1960 (R. 251-341). The first part of the opinion is devoted to an analysis of the feasibility of regulating independent natural gas producer rates through use of individual company costs and investment (R. 258-266). Consistent with Respondent's previously expressed distaste for producer regulation,[3] the opinion recites the purported difficulties and unsolved problems which, according to Respondent, were the inevitable result of employing a cost-investment rate base as a starting point in regulating natural gas producers. After complaining of the clogged condition of its dockets, Respondent concluded that it would be neither administratively nor economically sound to utilize individual producer costs to fix independent producer rates (R. 265).

While prospectively rejecting future reliance on individual producer costs, Respondent's opinion noted that cost-based regulation was "clearly a lawful way to determine rates for Phillips . . . and under the present record is the only possible method." (R. 269).

Finding that the "jurisdictional cost of service for . . . [1956] was not very different from 1954" (R. 272), Respondent adopted the 1954 test year employed by the Examiner and proceeded to find Phillips' jurisdictional

[3] FPC, 35th Annual Report (1955), 177;
FPC, 37th Annual Report (1957), 17-18, 25;
FPC, 38th Annual Report (1958), 16-17;
FPC, 39th Annual Report (1959), 12-13, 18-19;
FPC, 40th Annual Report (1960), 17.

cost of service to be $54.5 million[4] subject to adjustment for purchased gas costs, gathering taxes and royalties, or 11.1¢ per Mcf on jurisdictional sales of 491,178,953 Mcf (R. 404). Jurisdictional revenues for 1954 were $45.6 million, resulting in an $8.9 million deficit for that year; the 1954 revenues do not include, of course, additional revenues experienced in subsequent years from the Section 4(e) increases consolidated with the rate investigation, from other Section 4(e) increases, from additional sales volume, and from new sales at higher prices.

Expressly relying upon unidentified extra-record "knowledge . . . that costs and prices of gas in the field have greatly increased since that time," Respondent, after concluding that Phillips' rates were not excessive in 1954, inferred without record support that they were "probably" not excessive through 1958—by which date it recognized that "very substantial further rate increases were filed by Phillips" (R. 324-329). Since it had also concluded that "there is nothing in the record to show that these past rates . . . are unduly discriminatory or preferential" (R. 325), Respondent terminated all but two of the Section 4(e) proceedings[5] and discharged Phillips from further refund obligation, thereby approving existing[6] and increased rates during the 1957-1959 period, based solely on 1954 costs and revenues.

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[4] As revised in the order denying rehearing (R. 401).

[5] The rates called for by the rate schedules involved in Docket Nos. G-10883 and G-11217 are subject to revision on contractual grounds upon the decision of certain pending pipeline rate cases, and hence these dockets were held open on this limited issue (R. 326-28).

[6] Regularly since 1954, Respondent has authorized all producers, including Phillips, to undertake new sales at initial prices more than double the 1954 average price; its justification for not scrutinizing the justness of these prices was that they would eventually be reviewed in the Section 5(a) investigations, where they could be prospectively lowered.

With regard to the Section 5 investigation, involving Phillips' future rates, Respondent recognized that "the next step would ordinarily be to alter Phillips' rates . . . prospectively . . ." (R. 323). Notwithstanding the pendency of some 95 substantial rate increases filed by Phillips (R. 324, 329),[7] however, Respondent terminated without further action the general Section 5(a) rate investigation. This action was justified on two principal grounds: (1) that it would be "a result without reason or justice" to fix Phillips' 1960 rates upon data for an earlier test year (R. 325),[8] and (2) that "the interest of consumers and the exigencies of regulation will be better served in rate proceedings brought on an area basis rather than on an individual company basis" (R. 397).

Statement of General Policy No. 61-1—Concurrently with its opinion herein, Respondent issued a Statement of General Policy No. 61-1, 25 Fed. Reg. 9578, containing two lists of area prices, one for initial rates for issuing certificates under Section 7 and another for increased rates (under Section 4(e)) for gas sold under existing contracts, for use "as a guide to us [the Commission] and to interested parties in determining whether proposed initial rates should be certificated without price condition and whether proposed rate changes should be accepted or suspended" (R. 343). Respondent expressly represented, however, that the guides were tentative and did not propose to establish "just and reasonable" rate levels for Phillips or any other producer (R. 266, 346). The Policy Statement was issued without notice, hearing or record,

[7] As the opinion itself points out, the total annual impact of just five of these increases is approximately $11,000,000 (R. 324, n. 43).

[8] This point was abandoned by counsel for Respondent at the argument in the court below.

and has been amended several times since, also without notice, hearing or record.

Decision of the court below—On November 30, 1961, the Court of Appeals for the District of Columbia Circuit, Judge Fahy dissenting, sustained the Commission and affirmed its order.

At the outset of its opinion, the court recognized that it was confronting a problem of major importance, stating, "Some controversies concern major problems of general application. Others concern only a limited set of circumstances. The case at bar is of the former variety." (App. A, *infra*, p. A3.)

The court found that three time periods were involved. The first covered the "locked in" period, running from February 1955 through July 1959, during which certain of Phillips' rates were subject to refund under the twelve Section 4(e) dockets. The second covered the period of Phillips' "current rates", that is, rates being charged in 1959 and thereafter until such time as the Commission's proposed area rate making procedures are formulated and placed into effect. The third time period follows completion of the proposed area rate proceedings, at which time rates for the future would be established by reference to the new area standard.

Considering the first time period, the majority held that the Commission had properly allowed Phillips' rate increases to become effective for the 1955-1959 period solely on the basis of its determination of 1954 costs and revenues.[9]

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[9] As Petitioners point out, *infra*, p. 23, the majority seems to have overlooked the fact that the Commission had no record support for its implied finding that the 1955-1959 rate increases were "just and reasonable." See *Smith* v. *Illinois Bell Tel. Co.*, 282 U.S. 133 at 161-2 (1930).

After a brief discussion of the third period, involving Respondent's projected treatment of "future" rates in the proposed area proceedings,[10] the court then turned to the middle of the three time periods, that involving "current" rates. The court recognized that the "current" period could last as long as fourteen years and that Respondent is obligated to protect consumers during this period by some form of interim regulation. Although Respondent had proposed to defer regulation of existing rates indefinitely, the majority suggests that the Commission will be able to use its SGP61-1 rates during this period to test the reasonableness of existing rates as well as to test proposed initial rates or to decide whether to suspend and investigate rate increases.[11]

Since the SGP61-1 rates had been adopted without notice, hearing, record or specific findings, and appear to be based primarily on existing field prices (*infra*, pp. 15-16), the court, as a necessary support for its conclusions, held (1) that the Commission could lawfully base its determination of just and reasonable rates on field price data alone without reference to the financial requirements of the producers (App. A, *infra*, pp. A16-A18), and (2) that the SGP61-1 temporary rate levels were in fact "just and reasonable" rates which could be used for this purpose, subject

[10] Inasmuch as the Commission's plans for area proceedings are "now in an inchoate status" (App. A, *infra*, pp. A21-A22), any consideration of the validity of such a procedure would be premature at this time. See *infra*, p. 14.

[11] The court states (App. A, *infra*, p. A18) that "the new method [i. e., the SGP61-1 interim rates] will also apply in 5(a) proceedings to any existing rate found to be unjust or unreasonable." As we shall show, *infra*, p. 15, the court here misconceives the purpose of the SGP61-1 levels, which were not intended by the Commission to be used in determining just and reasonable rates in Section 5(a) proceedings, but solely to determine whether or not to suspend and investigate rate increases under Section 4 and to determine the lawfulness of initial rates in proceedings under Section 7 of the Natural Gas Act, 15 U.S.C. 717f.

to challenge in individual rate proceedings (App. A, *infra*, p. A17).

Finally, the court, after pointing out that "the Commission has found that present rates result in deficits to the company",[12] concluded that the Commission's order was valid and should be affirmed.

Judge Fahy dissented[13] (App. A, *infra*, pp. A20-A23). He pointed out that Respondent's opinion demonstrated the feasibility of deciding the Phillips' Sections 5(a) and 4(e) cases on the basis of the existing record, supplemented as necessary; that the majority should not have attempted to settle the validity of the area rate method since that question was not properly before it; that the result of the Commission's action would be to leave Phillips' rates unregulated for the indefinite future, which is entirely inconsistent with the mandate of the Natural Gas Act; that a Commission decision on the record, supplemented as necessary by more recent data, would be far more consistent with the mandate of the Act than the Commission's actual termination of the proceedings based on 1954 data; that the Commission could not dispose of the issue as to the justness and reasonableness of the present 1960-1961 rates on the basis of the 1954 data; that a decision in this case would not preclude the Commission from embarking on an area rate making program; and that the results of the Section 5(a) proceedings presently nearing completion before the Commission could provide assistance to the Commission in establishing guides of the SGP61-1 type, pending the completion of the area proceedings.

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[12] This is an inadvertent misstatement of the record, inasmuch as Respondent's finding was based on Phillips' 1954 costs as compared with its 1954 rates, and Respondent expressly refused to require Phillips to submit current cost and revenue figures relating to the "present" period of 1960-61. (R. 396-7).

[13] With partial concurrence on a point not raised by Petitioners herein.

Reasons for Granting the Writ.

The majority decision below emphasizes (App. A, *infra*, p. A3) that this is a case of major importance, involving one of the most significant Federal regulatory issues to come to this Court in a decade. Subsequent to this Court's *Phillips* decision in 1954, the major unresolved problem of Federal Power Commission regulation has been the fixing of just and reasonable producer rates. Since *Phillips*, the average field price of gas has risen over 60 percent and is continuing to rise rapidly; all of this increase is, of course, paid by the ultimate consumer. Because the FPC's rate-making powers, to the extent pertinent here, are predominantly prospective and cannot reach back to require disgorgement of present and past excesses, all delay in fixing just and reasonable producer rates works to the detriment of the consuming public.

The decision below would permit the Federal Power Commission, without good and sufficient reason, to defer resolution of the producer rate problem for an indefinite period, estimated at not less than four years and extending perhaps as much as fourteen years. The decision below will thus cause enormous and irreparable injury to ultimate consumers of natural gas for an indefinite future period.

Further, the decision below would permit a regulatory agency to achieve a prohibited abdication of jurisdiction by adopting a policy which amounts to an indefinite deferral of exercise of jurisdiction. Discretion an agency has; but not the discretion to repeal its statutory grant of power.

We submit, furthermore, that the decision below is squarely in conflict with earlier decisions of the same court of appeals and is inconsistent with other decisions of that and another court of appeals, as well as with two decisions of this Court.

1. Indefinite Deferral of Effective Regulation.

The purpose of the Natural Gas Act is, as this Court has frequently held, to protect the consumer from exploitation at the hands of the natural gas company. *FPC* v. *Hope Natural Gas Co.*, 320 U.S. 591, 610 (1944); *Sunray Mid-Continent Oil Co.* v. *FPC*, 364 U.S. 137, 147 (1960). To achieve this purpose, the Federal Power Commission has been endowed with substantial regulatory jurisdiction over the natural gas industry, and has, as a regulatory agency should, considerable discretion in the exercise of its jurisdiction. But both the scope and the exercise of the Commission's jurisdiction must be interpreted in light of the Commission's primary statutory purpose—consumer protection. *FPC* v. *Transcontinental Gas Pipe Line*, 365 U.S. 1 (1961) (FPC's broad interpretation of its jurisdiction upheld); cf. *Phillips Petroleum Company* v. *Wisconsin*, 347 U.S. 672 (1954) (FPC's narrow interpretation of its jurisdiction reversed). *FPC* v. *Hope Natural Gas Co.*, 320 U.S. 591 (1944) (FPC action upheld as within the allowable scope of agency discretion); cf. *Atlantic Refining Company* v. *Public Service Commission of New York*, 360 U.S. 378 (1959), and *City of Detroit* v. *FPC*, 230 F. 2d 810 (D.C. Cir. 1955), cert. den. 352 U.S. 829 (FPC action reversed notwithstanding agency's claim of discretion to select a regulatory method).

The vice of the Commission's decision is that it deprives the consumer of the "complete, permanent and effective bond of protection"[14] which the Natural Gas Act intended; specifically, the right to be free from excessive rates for natural gas.

Upon being told by this Court in 1954 that producers selling natural gas for resale in interstate commerce were subject to regulation under the Natural Gas Act, respond-

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[14] *Atlantic Refining Co.* v. *Public Service Commission of New York*, 360 U.S. 378, 388 (1959).

ent's responsibilities fell into two major categories. First, it was obliged to fix, as rapidly as possible, the just and reasonable rate for producer sales—a task then sixteen years overdue. Second, since it was evident that the ultimate fixing of producer rates would take some time, respondent was under an obligation to maintain control over price levels until it could, by completing its first task, determine whether adjustments were necessary. The two items were, of course, interrelated. The longer respondent took to fix just and reasonable rates, the more important interim price-protection measures became, *Atlantic Refining Company* v. *Public Service Commission of New York*, 360 U.S. 378; and the less effective respondent's efforts to stabilize prices during the period when just and reasonable rates were being determined, the more important speed in fixing rates became.

Unfortunately, respondent neither stabilized the price level pending ultimate conclusion of the rate proceedings—from 1954 to 1960, the average price of gas sold by producers to interstate pipelines advanced from 9.9¢ to 15.6¢ per Mcf[15]—nor did it move with speed in its rate-fixing proceedings. Respondent's more egregious failures to make any effort at stabilizing prices have twice been reversed by this Court and six times by courts of appeals,[16] and the imperceptible forward motion of respon-

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[15] The 1954 level of 9.9¢ represented an all-time high, and compares with a range of 4.5¢-6.5¢ between 1938 and 1950.

[16] *Atlantic Refining Co.* v. *Public Service Commission of New York*, 360 U.S. 378 (1959); *Public Service Commission of New York* v. *FPC*, 361 U.S. 195 (1959); *United Gas Improvement* v. *FPC*, 283 F.2d 817 (9th Cir. 1960), cert. denied 365 U.S. 879, 881; *Public Service Commission of New York* v. *FPC*, 287 F.2d 146 (D. C. Cir., 1960), cert. denied 365 U.S. 880, 882; *Public Service Commission of New York* v. *FPC*, 287 F.2d 143 (D. C. Cir., 1960); *United Gas Improvement* v. *FPC*, 287 F.2d 159 (10th Cir., 1961); *United Gas Improvement* v. *FPC*, 290 F.2d 133 (5th Cir., 1961), cert. denied, 368 U.S. 823; *United Gas Improvement* v. *FPC*, 290 F.2d 147 (5th Cir., 1961), cert. denied, 366 U.S. 965.

dent's rate proceedings have twice drawn comment from this Court.[17]

Nonetheless, by the fall of 1960, the Phillips rate proceeding *was* ready for decision, and the Section 5(a) rate proceedings of a half dozen other major producers were nearing conclusion. It was at this juncture that respondent decided to drop the individual-company cost-of-service method employed by all parties in all the pending cases and embark instead upon a new method (in essence a multi-company cost-of-service method). Assuming *arguendo* that the new method constitutes a desirable and legal way of fixing producer rates, the decision defers effective rate-fixing for another four years at least. And if the Commission has as broad discretion as the decision below suggests, when all the preliminary stages incident to the new method have been completed and the Commission is again on the brink of decision, it could presumably decide that a third method might be still better, and terminate the area proceedings without arriving at a definitive result.

The court below, of course, recognized that there is a "need for interim regulation." To meet this need, it asserted (App. A, *infra*, pp. A14, A18) that the Commission's temporary "area prices" (promulgated in its Statement of General Policy No. 61-1, hereafter SGP61-1) can and will be applied to existing and future rates under Section 5(a) so as to protect consumers against unjust and unreasonable average rate levels pending completion of the area proceedings. Thus, the court below apparently believed that Respondent intended in SGP61-1 to adopt (at least during the interim) a variation of the "fair field price" regulatory method for which Respondent has sought authorization so often and so fruitlessly from Congress.[18]

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[17] 360 U.S. 378, 389-90; 364 U.S. 137, 144-5.

[18] See fn. 3, *supra*.

This is a fundamental misconception, since SGP61-1 itself makes clear (R. 343) that the 61-1 rates are to be used *only* in conditioning initial prices under Section 7 of the Act and in suspending (but not testing) increased rates under Section 4(e)—not in setting just and reasonable rates under Section 5(a). This is confirmed by other Commission statements, most recently in Respondent's Opinion No. 350 issued over a month after the decision below, stating that "The area price levels, as set forth in the Policy Statement and its amendments, are 'for the purpose of guidance and initial action by the Commission,' and do not constitute determinations of just and reasonable prices."[19]

The court below not only misunderstood what the SGP levels were, equally important, it misunderstood how they were computed. Thus, the court states that the levels were based on Respondent's "own judgment and accumulated data" and "on the basis of the internal data in its files on all the operators in the several areas." While this suggests that the data on which the SGP levels are based include producer expense data, Appendix D demonstrates that the SGP61-1 prices in each case are merely the highest previously permanently certificated and wholly unregulated price in each area as of September 1960 when SGP61-1 was issued. And as one leading authority has commented, "the area prices . . . come close to approximately current

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[19] *Panhandle Eastern Pipeline Co.*, Opinion No. 350, January 15, 1962, 27 F.P.C. ; Mimeo., p. 9. Since the SGP levels were issued without hearings, record or findings of any kind, and since they appear to be based largely, if not exclusively, on unregulated field prices, it is hardly likely that Respondent could or would attempt to employ them to reduce existing or future rates to "just and reasonable" levels. *Ohio-Bell Telephone Co.* v. *Public Utilities Comm'n of Ohio*, 301 U.S. 292; *Colorado-Wyoming Gas Co.* v. *F.P.C.*, 324 U.S. 626, 633-635; *I.C.C.* v. *J-T Transport Co.*, 368 U.S. 81. This is no doubt why Respondent has repeatedly disclaimed any intention of using the 61-1 rate levels other than as a guide to its discretion in conditioning initial prices or in suspending and investigating increased rates.

maximum prices, which have more than doubled in the past five years.'"[20]

There are, of course, many areas in which the Commission's files, internal or otherwise, would furnish data which could be used in appropriate cases—the cost of transporting an Mcf of gas 100 miles through 24-inch pipe, for example. But the recordation in the Commission's files of prices which have been or are being paid does not validate as a method of price regulation the otherwise invalid "fair field price" doctrine. See further, *infra*, pp. 17-20.

We noted above that although area prices are ultimately intended to reflect industry-wide cost experience, the SGP levels reflect only current prices being paid. As Judge Fahy, dissenting below, pointed out, if the Commission were to fix rates in the Phillips and related rate investigations on the basis of the individual-company cost experience in the respective records, supplemented as necessary, it could accumulate the very type of cost-experience data necessary to establish price guides which *would* reflect just and reasonable prices. Thus, completion of the individual company cases, far from impeding the area price venture, would move it forward.

2. Abdication of Jurisdiction.

In its original 1951 decision in this proceeding, 10 F.P.C. 246, respondent held that it lacked power to regulate sales made by producers for resale in interstate commerce. As noted, that holding was reversed as an error of law by the Court of Appeals, 205 F.2d 706 (D.C. Cir. 1953) and by this Court, 347 U.S. 672 (1954). Thereafter, Respondent repeatedly asked Congress to amend the Natural Gas Act to exempt producers or to relax producer regulation.[21]

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[20] Landis, *Report on Regulatory Agencies to the President-Elect*, p. 55 (1960).

[21] See fn. 3, *supra*.

Respondent's 1960 opinion, affirmed by the decision below, would achieve a substantial portion of the abnegation of power disapproved by this Court and subsequently refused by Congress. Section 4(a) provides "All rates and charges made, demanded, or received by any natural gas company for ... the ... sale of natural gas subject to the jurisdiction of the Commission, ... shall be just and reasonable, and any such rate or charge that is not just and reasonable is hereby declared to be unlawful," and Section 5(a) requires that "Whenever the Commission ... shall find that any rate ... charged ... by any natural-gas company ... is unjust [or] unreasonable, ... the Commission shall determine the just and reasonable rate ... to be thereafter observed and in force, and shall fix the same by order."

In deferring producer regulation under Sections 4 and 5(a) for an indefinite period, the Commission has abdicated its basic regulatory functions under the Natural Gas Act. Its discretion to select a regulatory method does not permit it to abdicate its total regulatory responsibilities for a substantial period. The freedom from regulatory responsibility which the Respondent could not achieve as a matter of law the first time around, it should not be permitted to achieve as a matter of discretion nine years later in the same proceeding. The mandate of the Natural Gas Act to protect consumers is so strong that, in a period of rapidly rising field prices, Respondent has no discretion to put off its regulation until another day.

This generation of consumers, as well as the next, is entitled to protection.

3. Conflict With Other Decisions.

a. Consideration by this Court is necessary on the independent ground that the holding below conflicts squarely

with *City of Detroit* v. *F.P.C.*, 230 F.2d 810 (D.C. Cir. 1955), *cert. denied*, 352 U.S. 829; and *Mississippi River Fuel Corp.* v. *F.P.C.*, 252 F.2d 619 (D.C. Cir. 1957), *cert. denied*, 355 U.S. 904; and conflicts in substance with *Episcopal Theological Seminary* v. *F.P.C.*, 269 F.2d 228 (D.C. Cir. 1959), *cert. denied*, 361 U.S. 895; *Bel Oil Co.* v. *F.P.C.*, 255 F.2d 548 (5th Cir. 1958), *cert. denied*, 358 U.S. 804; *Forest Oil Co.* v. *F.P.C.*, 263 F.2d 622 (5th Cir. 1959); and *United Gas Improvement Co.* v. *F.P.C.*, 290 F.2d 133 (5th Cir. 1961), *cert. denied*, 368 U.S. 823.

The majority appears to hold that Respondent may rely upon "fair field prices" (i.e., unregulated prices set by existing market forces) in determining "just and reasonable" rates, without consideration of the producers' financial requirements (App. A, *infra*, p. A17). The court was presumably driven to this conclusion because it recognized that the interim area rates were based largely on unregulated field prices, and it could not hold that these rates are just and reasonable without also holding that Respondent need not consider producer costs or financial requirements even as a starting or comparison point in producer regulation.

The District of Columbia Circuit in *City of Detroit*, *supra*, 230 F.2d at 815-819, has held that the Commission could not, in determining just and reasonable rates for a pipeline which produced its own gas, allow the pipeline the fair field price (i.e., the going market price) for its gas without at least considering the pipeline's production costs as a check on whether fair field price would be excessive or exorbitant under the standards of the Act. This holding was subsequently applied to producer rates paid by an interstate pipeline company and claimed as a cost of service in *Mississippi River Fuel*, *supra*, 252 F.2d at 623 (reaffirmed,

Willmut Gas & Oil Co. v. F.P.C., F.2d (No. 16,245, D.C. Cir. 1962)).

The decision below conflicts squarely with these decisions in its holding that Respondent can set just and reasonable producer rates based solely on (App. A, *infra*, p. A16):

> "• • • the fair prices for the product as measured by the open competitive market for the product, evaluated by Commission expertise and data on the whole of the market operation."

In its holding on fair field price, the decision below also conflicts with the following decisions[22] involving Commission review of independent producer rates under Section 4(e) of the Natural Gas Act:

Bel Oil, supra, (255 F. 2d at 548):

> "• • • We do not hold that evidence of field price is irrelevant. We do hold that evidence of unregulated prices in the field is not sufficient to warrant a finding by the Commission that a price comparable to them is just and reasonable within the intendment of the Natural Gas Act. Neither is evidence of the field price when coupled with the opinion of experts that the price must be high enough to provide an incentive for exploration and development of new sources of supply."

(This holding is expressly reaffirmed in *Forest Oil Co. v. F.P.C.*, 263 F. 2d 622 (5th Cir. 1959); and *United Gas Improvement Co. v. F.P.C.*, 290 F. 2d 133, 135 (5th Cir. 1961)).

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[22] These decisions recognize, as did *City of Detroit, supra*, that the Commission is not *required* to employ a cost of service-rate base method of setting producer rates, but hold that "fair field price", alone, without consideration of financial requirements, does not meet the standards of the Act.

Episcopal Theological Seminary v. *F.P.C.*, 269 F. 2d 228, 236 (D.C. Cir. 1959), by Reed, Associate Justice (emphasis added):

> "What the Commission has done is to say that petitioners must make a showing as to its operations. It seems to us reasonable to make such a requirement. The primary aim of the Natural Gas Act is 'to protect consumers against exploitation at the hands of natural gas companies.' One aid to such an aim is to weigh the needs of the gas companies by an examination of its costs and profits. What better test could there be as to the reasonableness of existing or proposed rates to a company than a careful analysis of the evidence as to its recent earnings? *That is one of the elements of any rate-testing method.* [Footnotes omitted.]

See also *Public Service Comm'n of New York* v. *F.P.C.*, 287 F. 2d 146, 149 (D.C. Cir. 1960), cert. denied, 365 U. S. 880, 882.

The issue raised by this conflict is of continuing importance, and should be resolved by this Court. The Natural Gas Act by definition constitutes a legislative finding that competition alone cannot be relied upon to insure reasonable rates in the natural gas industry, *United Gas Improvement Co.* v. *F.P.C.*, 290 F. 2d 133, 135 (5th Cir. 1961); and we have noted earlier (*supra*, p. 16) that Congress has repeatedly refused to amend the Act to adopt a "fair field price" standard. The majority, in its statement quoted, *supra*, p. 19, does not explain how Respondent would be able to "evaluate" open market prices in the absence of any evidence of producer financial requirement; and it seems obvious that Respondent would have to approve uncritically as just and reasonable whatever the predominant field price level is at any time.

b. In holding that Respondent may decline to fix just and reasonable producer rates for yet another four years or more, the decision below is inconsistent with this Court's decision in *Phillips Petroleum Company* v. *Wisconsin*, 347 U. S. 672 (1954). See *supra*, pp. 12-13. While Respondent is entitled to a reasonable time within which to comply with this Court's mandate in Phillips, we would point out that almost eight years have elapsed since this Court directed Respondent to fix just and reasonable rates for *Phillips;* that Respondent has yet to fix such rates; and that the decision below would permit Respondent to defer indefinitely its obligation to fix rates for Phillips.

c. In holding that Respondent has no obligation to proceed with due diligence in the promulgation of interim relief pending ultimate determination of the producer rate problem, the decision below is inconsistent with this Court's decision in *Atlantic Refining Company* v. *Public Service Commission of New York*, 360 U. S. 378 (1959), a case which bears striking parallels to the instant proceeding.

In *Atlantic Refining*, the Federal Power Commission sought to defer action on a proposed high price for a new producer sale from the certificate proceedings, where the matter was ripe for interim action, to a subsequent rate investigation under Section 5; the Commission defended such postponement on the ground that the Section 5 proceeding would afford a more appropriate forum for the disposition of a rate issue. This Court disagreed. Finding that "the overriding intent of the Congress to give full protective coverage to the consumer as to price" would be defeated if potentially excessive prices were permitted to remain effective during the extensive time period

necessary to conclude a Section 5 proceeding, this Court held that the Commission was obligated to give careful scrutiny to the rate proposals in the certificate case. The Court stated:

> "The Act was so framed as to afford consumers a complete, permanent and effective bond of protection from excessive rates and charges . . . .
>
> "In view of this framework in which the Commission is authorized and directed to act, the initial certificating of a proposal under Section 7(e) of the Act as being required by the public convenience and necessity becomes crucial. This is true because the delay incident to determination in Section 5 proceedings through which initial certificated rates are reviewable appears nigh interminable. Although *Phillips Petroleum Co.* v. *Wisconsin*, 347 U.S. 672, was decided in 1954, cases instituted under Section 5 are still in the investigation stage. This long delay, without the protection of refund, as is possible in a §4 proceeding, would provide a windfall for the natural gas company with a consequent squall for the consumers. This the Congress did not intend." 360 U.S. at 388-390.

Thus the specific holding in *Atlantic Refining* was that the Commission may not defer action on a rate problem until a Section 5 proceeding but must act on that problem when first presented in a Section 7 certificate proceeding. The *lesson* of *Atlantic Refining*, however, is that where the Commission has the choice of following two regulatory routes, one of which can be pursued promptly and the other of which will take many years for conclusion, it must follow the faster where the consumer will be injured by delay. In *Atlantic Refining*, action in the Section 7 proceeding afforded much prompter relief than action at the conclusion of a "nigh interminable" Section 5 proceeding; here,

action in the already completed Section 5 proceeding would afford much prompter relief than action at the conclusion of a not-yet-started area rate proceeding.

4. Impact on Consumer.

The impact of the decision below on the consuming public is enormous.

a. Between Respondent's 1951 determination that it lacked jurisdiction and its 1960 determination whereby it did not effectively exercise jurisdiction, the average price of gas more than doubled, from 7.3 cents per Mcf to 15.6 cents per Mcf. In terms of impact this means that in 1960 ultimate consumers of natural gas paid producers approximately $1,000,000,000 more than they would have had the 1951 field prices continued in effect; of this total, over 60 percent was paid by interstate consumers.

The recent rapid rise of producer prices — in which Phillips has shared—makes immediate relief essential. For example, between 1954 and 1960 Phillips' average unit revenues increased from 8.9 cents per Mcf to 14.3 cents per Mcf; the only evidence in this record of cost trends indicates that Phillips' unit costs *decreased* from 1954 to 1956.[22a]

Although the court below held that consumers had "no tenable grounds for complaint" of Phillips' present rates because the Commission "has found, after elaborate consideration, that *present* rates result in deficits to the company," the Commission in fact made no such finding. Rather, it found that Phillips' *1954* rates resulted in deficits to the Company in 1954. But since 1954, Phillips' sales have increased 30 percent, its average unit revenues have increased 60 percent, and its total jurisdictional revenues

[22a] As determined by Phillips on a consistent basis in Exhibits 282 and 303. See R. 86-88.

have more than doubled.[23] It is Petitioners' contention that under the cost-finding methods used by Respondent in this proceeding, Phillips' *present* rates are almost certainly excessive, and that a supplemental hearing, to compare Phillips' present revenues with its present costs, should be held.[24]

As Judge Fahy makes clear in his dissent below, the only presently available way of insuring that consumers will not pay exorbitant rates during the coming eight to ten years is for Respondent to utilize the records in the almost-completed thirteen major producer rate cases (including Phillips) to appraise the justness and reasonableness of existing sharply increased rate levels. It is entirely feasible for Respondent to do this, since the proceedings are virtually completed, and as the dissent points out (App. A, *infra*, p. A22): "The Commission has come so close to doing what it says it should not do as to demonstrate that it is able to do what it has failed to do."[25]

The majority below suggests that decision of these cases under Section 5(a) will offer no greater protection than that which *could* come out of the area rate proceedings, provided they are successfully completed.[26] Needless to

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[23] 1954 data from FPC Opinion 338; 1960 data from FPC staff report on 1960 producer sales, issued October 1961.

[24] Since the Phillips cost-finding methods have been determined, this would require only submittal of current cost data from Phillips' books. From the administrative standpoint, the relative ease with which this could be accomplished is demonstrated by the "Phillips-type" cost-of-service presentations made by the FPC Staff and other parties in each of the related rate investigations following this issuance of Respondent's Opinion 338 (Appendix C, *infra*).

[25] Hearings have been completed in all but one of the thirteen cases, and the final briefs have been submitted in all but five.

[26] "The new method will also apply in 5(a) proceedings to any existing rate found to be unjust or unreasonable. Refunds cannot be ordered in the latter cases and so consumers bear the disputed rates during the period of the inquiry. But this same situation obtains in the present process of regulation; the application of the new criteria makes no change in this procedural aspect." (App. A, *infra*, p. A18).

say, this overlooks the crucial fact that the existing producer cases admittedly could be decided in a relatively short time: the terminal dates of the area proceedings are speculative, but in any event, many years in the future.

Decision of the thirteen pending cases would offer substantial relief to the consumer in two ways. Appendix C, *infra*, demonstrates that this case alone involves rates governing nearing one-tenth of the natural gas sales subject to the Commission's jurisdiction, and that over 30% of jurisdictional sales by volumes and by revenue is the subject of current producer rate cases in which hearings have been concluded.[27] Thus, the Commission has the power directly within its grasp to provide substantial relief for the nation's rate payers simply by acting on the cases now before it.

Further, past experience indicates that rates set in these cases would provide a strong stimulus for settlement of other pending cases, and adjustment of producer rates generally to reasonable levels during the interim period pending completion of the area proceedings.[27]

b. The upward movement of producer prices has, of course, been the primary cause of rate increase filings by the pipeline purchasers,[28] leading to what the Commission has told this Court is "a serious backlog of cases".[29] In *F.P.C.* v. *Tennessee Gas Transmission*, this term No. 591, certiorari granted, respondent noted, "Pipeline rate increases have become more and more frequent in recent years." (Petition for certiorari, p. 19). In the *Tennessee*

[27] FPC Staff report on 1960 producer sales, issued October 1961.

[28] FPC Annual Reports, 1957, p. 82, 1958, p. 73; 1959, p. 79; 1960, p. 75.

[29] FPC petition for certiorari, *FPC* v. *Tennessee Gas Transmission*, this term No. 591, p. 20.

Gas case, which is fairly typical, the pipeline has since 1954 filed four increases which amount to almost $80,000,000 on an annual basis. Of this total, $56,000,000, or over 70 percent, is attributable to the rise in the pipeline's cost of purchased gas—the proper determination of which is the very problem here involved.[30] The problem of pipeline rate backlogs is a serious one, and the aspect of that problem raised by the *Tennessee* case—prompt disposition of specific issues to permit immediate partial refunds—is of real importance. But the *primary* cause of the pipeline rate problem is continued postponement of producer rate regulation—the issue presented here. *A fortiori* this case warrants certiorari.

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[30] The issue in the pending *Tennessee* appeal is whether the Federal Power Commission has power, in the circumstances, to trim Tennessee's rates by $11,000,000 annually to reflect a rate of return finding adverse to the pipeline. In dollar impact on the Tennessee system, the cost of purchased gas issue bulks five times as large as the issue involved in the pending *Tennessee* appeal.

Conclusion.

For the foregoing reasons, it is respectfully submitted that this petition for a writ of certiorari should be granted.

Dated, February 27, 1962.

Respectfully submitted,

JOHN W. REYNOLDS,
Attorney General, State of Wisconsin,

ROY G. TULANE,
Assistant Attorney General, State of Wisconsin,
State Capitol,
Madison 2, Wisconsin,
Attorneys for State of Wisconsin.

WILLIAM E. TORKELSON,
Chief Counsel, Public Service Commission of Wisconsin,
State Office Building,
Madison 2, Wisconsin,
Attorney for Public Service Commission of Wisconsin.

KENT H. BROWN,
Counsel, Public Service Commission of the State of New York,
55 Elk Street,
Albany 1, New York.

BARBARA M. SUCHOW,
Assistant Counsel, Public Service Commission of the State of New York,
120 Church Street,
New York 7, N. Y.

MORTON L. SIMONS,
1815 H Street, N. W.,
Washington 6, D. C.
Attorneys for Public Service Commission of the State of New York.

APPENDIX A.

Opinion of Court of Appeals.

UNITED STATES COURT OF APPEALS

FOR THE DISTRICT OF COLUMBIA CIRCUIT

No. 16175

STATE OF WISCONSIN and PUBLIC SERVICE COMMISSION OF WISCONSIN,

Petitioners,

v.

FEDERAL POWER COMMISSION,

Respondent,

PHILLIPS PETROLEUM COMPANY,

Intervenor.

No. 16177

LONG ISLAND LIGHTING COMPANY, *et al.*,

Petitioners,

v.

FEDERAL POWER COMMISSION,

Respondent,

PHILLIPS PETROLEUM COMPANY,
PUBLIC SERVICE COMMISSION OF THE STATE OF NEW YORK,

Intervenors.

No. 16180

PEOPLE OF THE STATE OF CALIFORNIA and PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA,

Petitioners,

v.

FEDERAL POWER COMMISSION,

Respondent,

PHILLIPS PETROLEUM COMPANY,

Intervenor.

ON PETITIONS FOR REVIEW OF ORDER OF THE FEDERAL POWER COMMISSION.

Decided November 30, 1961

Mr. WILLIAM E. TORKELSON for petitioners in No. 16175.

Mr. J. DAVID MANN, JR., with whom Messrs. JOHN E. HOLTZINGER, JR., WILLIAM W. ROSS, and DAVID K. KADANE were on the brief, for petitioners in No. 16177.

Mr. WILLIAM M. BENNETT for petitioners in No. 16180.

Mr. ARTHUR H. FRIBOURG, Attorney, Federal Power Commission, with whom Mr. JOHN C. MASON, General Counsel, Federal Power Commission, at the time the brief was filed, and now Deputy General Counsel, and Mr. HOWARD E. WAHRENBROCK, Solicitor, Federal Power Commission, were on the brief, for respondent.

Mr. KENNETH HEADY, of the bar of the Supreme Court of Oklahoma, *pro hac vice*, by special leave of court, with whom Messrs. CHARLES E. McGEE and LAMBERT McALLISTER were on the brief, for intervenor Phillips Petroleum Company.

Messrs. Kent H. Brown and George H. Kenny and Mrs. Barbara M. Sucnow were on the brief for intervenor Public Service Commission of the State of New York in No. 16177.

Before Prettyman, Fahy and Danaher, Circuit Judges.

Prettyman, Circuit Judge: Some controversies concern major problems of general application. Others concern only a limited set of circumstances. The case at bar is of the former variety. The questions are posed by complicated procedural difficulties. They concern the procedures of the Federal Power Commission in dealing with the rates of natural gas producers.

The Phillips Petroleum Company is a producer of natural gas. It procures gas from several widely separated and widely differing areas. It explores for, develops, produces, purchases, gathers and processes gas and oil. It sells gas to pipeline companies[1] under contracts negotiated by it and these customers. The contracts differ in such terms as delivery conditions, water content, hydrocarbon content, place of delivery, pressure, and price.

Two sections of the Natural Gas Act[2] are involved. One (Section 4(e)) provides in essence, as to sales subjected to regulation by the Commission, that when a rate or an increased rate is filed the Commission may suspend it for five months, meantime setting it for hearing. When such a rate goes into effect after the period of suspension (the Commission not having concluded its consideration), the funds derived from the newly-filed rates may be impounded and, in so far as the Commission fails to approve them, may be refunded. The burden of proving in such a proceeding that an increased rate is "just and reasonable" rests upon the company. The other section of the statute (5(a)) provides in essence that either upon a complaint or upon its own motion the Commission may inquire into an existing rate. If that rate be found unlawful the Commission must

[1] It also sells oil, products condensed from gas, and other petroleum products and chemicals. It sells natural gas in several conditions. It sells to customers other than pipelines as well.

[2] 52 Stat. 821 (1938), as amended, 15 U.S.C. §§ 717-717w.

determine what shall thereafter be decreed a just and reasonable rate. Its decision becomes effective from its date. No refund is involved.

In October, 1948, the Commission instituted a proceeding under Section 5(a), the latter of the above sections, concerning Phillips's rates. In that proceeding it decided it had no jurisdiction over the rates of producers of natural gas. This court reversed the Commission,[3] and the Supreme Court affirmed our decision.[4] The Commission reinstated its 5(a) proceeding.

Meantime and thereafter Phillips filed increased rates in respect to many of its contracts. The Commission suspended them and set them for hearing, under Section 4(e) of the statute, the first of the two sections above discussed. Many purchasers, many contracts, many rate schedules, and many filings were involved. Thus many 4(e) proceedings, under different docket numbers, were instituted. As time went on, Phillips filed further proposed increases in some of these same rates. In such event the earlier proposed rate would, if approved, cover a limited period, *i.e.*, until the succeeding increase in that same contract rate was filed. A period thus limited is called a "locked-in period" in the jargon of the industry. These later increases were also suspended by the Commission. Thus many proceedings under Section 4(e) involving rates of Phillips became pending.

The Commission consolidated the 5(a) proceeding and twelve of the 4(e) proceedings for hearing. These twelve 4(e) proceedings involved an aggregate of about five and a half million dollars in proposed increased rates. The proposed rates ranged from 5½ cents per Mcf to 13½ cents per Mcf. The proceeding was long, detailed, and resulted in a voluminous record of testimony and exhibits. The Examiner rendered a long (174 printed pages), careful and complete initial decision. He approached the

[3] *State of Wisconsin* v. *Federal Power Comm'n*, 92 U.S. App. D.C. 284, 205 F.2d 706 (1953).

[4] *Phillips Petroleum Co.* v. *Wisconsin*, 347 U.S. 672 (1954).

problem from the standpoint of cost-of-service[5] and rate base. Many perplexing problems were presented. He examined them all and decided them. Among them were different approaches to cost-of-service, the allocation of production costs, the allocation of exploration costs, the problem of natural gas liquids, the rate base, adjustment to the test year, the computation of the income tax component, the proper rate of return, working capital, allocations between jurisdictional and non-jurisdictional sales, field prices, a discussion of system-wide as compared with area rates. Upon all these the Examiner made detailed findings and conclusions, displaying commendable patience and grasp of the subject matter. He adopted a system-wide approach and found that Phillips's total jurisdictional cost of service, properly computed, was $57,280,218 for the test year,[6] or an average unit cost of 11.662 cents per Mcf. He recommended that Phillips be ordered to calculate a maximum rate for gas with certain described qualities at such level that, when applied to the sales volume for all jurisdictional contracts, adjusted for approved delivery condition differentials, would produce revenues roughly equal to the system-wide cost of service. He recommended that Phillips be ordered to file, with full explanations, a list of rates so calculated. These calculated rates would be subject to approval by the Commission. He recommended that the rates thus calculated and approved be applied in both the 4(e) and the 5(a) proceedings, *i.e.*, to both suspended and future rates.

The Commission reversed the Examiner. Its decision and findings were also extended and exhaustive (82 printed pages, plus exhibits). One Commissioner dissented in respect to the computation of the cost of service; otherwise he concurred. Basically, the Commission concluded "beyond any doubt, that the traditional original cost,

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[5] Cost-of-service in this context includes not only operating expenses, taxes, exploration allowances, and gas purchases but also a fair return on the rate base.

[6] Compared with 92.3 million dollars claimed by Phillips.

prudent investment rate base method of regulating utilities is not a sensible, or even a workable method of fixing the rates of independent producers of natural gas." It pointed out critical differences between pipeline operations and producer operations, quoting from opinions by Mr. Justice Harlan and Mr. Justice Jackson, and saying that in regulating producers it is faced with problems entirely different from those of an ordinary public utility. It pointed out that simply to allow producers a return on investment would penalize the efficient or fortunate and reward the inefficient or unfortunate. Only where a producer purchases a fully developed acreage at a fair price does his investment have a real relationship to his return. The producer who first takes the risk in an area and proves it productive pays less for his rights than those who come later. But he must invest his funds before he knows whether he will have anything to sell or not. Mr. Justice Jackson once wrote that "there is little more relation between the investment and the result than in a game of poker."

The Commission pointed out that a producer of natural gas also produces oil, the price of which is unregulated, makes sales (intrastate, etc.) not subject to Commission jurisdiction, and sells products also excluded. Thus "extremely difficult" problems of allocating costs are involved. It commented that none of the experts proposed allocations acceptable to other experts. "Ridiculous results will be reached among the great number of producers and owners of interests if costs should be the only basis for regulation." It referred to the fact that much of Phillips's gas is purchased from thousands of independent producers whose rates are under percentage-type casinghead contracts, dependent on Phillips's rates. The interests of the many royalty owners must also be considered. Another problem is the administrative burden of full cost rate cases for each of thousands of independent producers. Adherence to cost rate-base methods results in necessity for a full-scale company-wide cost study to determine the proper price in any one contract. At the time of this

Commission decision 3372 independent producers had rates on file. Five hundred seventy producers were involved in 3278 proposed rate increases under suspension and awaiting hearing. Of eleven rate increase cases in which full hearings had been had and decisions rendered, ten showed the increases justified. A special problem prevented decision in the other. In the three 5(a) cases theretofore completed, the producers' prices were found justified. Rigid adherence to the rate-base method would in many cases price the producers' gas out of the market. "From the foregoing, it follows that effective regulation of the price of natural gas must be on some more manageable plan than the rate base method. Thus it is clear that the better method would be to establish fair prices for the gas itself and not for each individual producer."

Simultaneously with the foregoing opinion the Commission promulgated a "policy statement" setting forth rate guidance schedules for various producing areas. These schedules consisted of two rates prescribed for each of twenty-three producing areas throughout the country (except for two areas, for which only one rate was given). One rate was for initial service, *i.e.*, new contracts, in the area. The other was for increases in rates, *i.e.*, proposals for increases in existing contracts, in the area. For example, in the first area listed (Texas District No. 1) an initial service rate of 15.0 cents per Mcf was given and an increased rate level of 14.0 cents per Mcf. The Commission described its preparation of these schedules thus:

> "In arriving at the price levels for the various areas set forth in the appendix to this statement, we have considered all of the relevant facts available to us. Such consideration included cost information from all decided and pending cases, existing and historical price structures, volumes of production, trends in production, price trends in the various areas over a number of years, trends in exploration and development, trends in demands, and the available markets for the gas. Of necessity, we have not

> set forth the adjustments to these prices which must be made to take into account every possible provision of every contract which may affect the actual price, such as Btu adjustments, conditions of delivery, etc. The relevance of such adjustments to the basic contract price and the appropriate established price standard must be considered as each filing is made."

The proposed use of this list was described by the Commission as follows:

> "* * * These standards will serve as a guide to us and to interested parties in determining whether proposed initial rates should be certificated without a price condition and whether proposed rate changes should be accepted or suspended.
>
> * * * * * *
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> "These price levels, as announced by Appendix A attached to this statement, are for the purpose of guidance and initial action by the Commission and their use will not deprive any party of substantive rights or fix the ultimate justness and reasonableness of any rate level."[7]

In its opinion the Commission said further: "This schedule of prices is only for guidance and does not constitute any determination of just and reasonable rates and will not foreclose any person from justifying a particular rate in any area." The schedule is of maximum acceptable rates for gas from a given area, as opposed to rates established for each rate filing by each producer after a full cost-rate base consideration of each rate so filed.

The Commission disposed of the consolidated cases before it in three parts. The first part consisted of the superseded rates of the prior periods ("locked-in" periods). The second consisted of the presently current rates and

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[7] Statement of General Policy No. 61-1, Sept. 28, 1960, 25 Fed. Reg. 9578 (Oct. 5, 1960).

those to be in effect during the interim period from now until the newly proposed area-rate system is completely designed and put into effect. The third part consisted of rates for the future after the completion and inauguration of the area-rate system.

Before we consider these several dispositions in detail we must understand the problem with which the Commission was dealing. The rates proposed to be increased in these 4(e) proceedings are not the rates of utilities in the traditional sense, such as pipelines. The rates here involved are the charges made by companies which buy or produce a product, process it to suit the requirements of a customer, and sell it to that customer under a contract. The product is procured from many different places, from Texas to West Virginia, from Louisiana to Wyoming. In its raw state it is of many different contents. Different customers require different terms as to the physical qualities of the delivered article, points and terms of delivery, and other factors. Hundreds of producers, hundreds of contracts, and thousands of rate filings are involved.

When we use the terms "cost of service" or "rate base" in this context, we must be careful of the meaning we intend. There is a system-wide cost of service. This would be, as the words indicate, a computation for the entire Phillips system. But even so it would not be a computation for all Phillips operations, because the Company has many operations, such as those in petro-chemical fields, and sales of all sorts of petroleum products, and many sales not subject to federal regulation under present statutes. In fact the Company's gross income from sales of natural gas in 1955 was less than six per cent of its total gross income. So even a system-wide computation of cost of service for sales of natural gas subject to Commission regulation requires monumental allocations of many costs, such as exploration costs, taxes, administration expenses, purchases, extraction costs, sales of residue gas and liquids, and so on. Nevertheless such a computation was made. The Examiner and also the

Commission determined and used a system-wide cost of service. As found by the Commission the system-wide cost of service for Phillips's sales of natural gas subject to Commission jurisdiction in the test year 1954 was $55,548,054, or 11.309 cents per Mcf. But even the figure thus carefully computed was subject to adjustment for purchased gas costs, gathering taxes, and royalties. The same observations apply to the rate base on a system-wide basis. One was determined by the Commission.

Then, theoretically at least, there is a cost of service for each contract, if not for each rate, and so for each 4(e) proceeding. But nobody, so far as we are advised, contends that any such computations could be made with any meaningful results by any known method. The results of any such effort would be pure guesswork, involving a vast multiplication of the arbitrary allocations which would have to be made.

The Examiner did not attempt to make any cost-of-service determination on individual contract, rate, or case basis. He determined a system-wide cost of service, which gave him a nationwide average unit cost of 11.662 cents per Mcf. He then proposed that "[b]ased on the system-wide cost of service herein approved, as set forth in Appendix Table 12 hereof, Phillips shall calculate the 'maximum rate for 1,000-pound, sweet, dehydrated, and gathered gas,' at such level that its application to the sales volumes delivered in 1954 under each and every one of the 1954 jurisdictional contracts, as adjusted for the approved delivery condition rate differentials, will produce total revenues roughly equal to such system-wide cost of service." He proposed further that "Phillips shall file with the Commission a statement of such 'maximum rate,' including a clear and detailed explanation as to the manner in which it was calculated, together with a list of *calculated rates* for all of its jurisdictional rate schedules then in effect." The Commission, as we have said, reversed the Examiner, treating the case, in effect, in three parts.

1. As to the first part of the problem, the 4(e) proceedings, dealing with suspended proposals now superseded, the Commission made system-wide conclusions as to jurisdictional sales and applied them to these cases. It found $45,568,291 of revenues against $55,548,054[8] cost of service. This showed a system-wide deficit of some $9,000,000 on jurisdictional sales of natural gas. The Commission noted that no evidence had been presented to show that the different rates in these different 4(e) proceedings were unduly discriminatory or preferential, which notation, translated, means that any adjustment in these rates should be correspondingly proportionate in respect to each and all. The Commission applied the result of its system-wide calculations to each and all of the 4(e) proceedings and concluded that no refunds were due. Having thus ordered, it concluded ("terminated") the proceedings.

The Commission made no determination of the cost of service of each of these contract rates separately; it had no evidence before it upon which it could make such determinations, and it was of opinion that such computations would be unworkable and foolish under the circumstances.

In these 4(e) cases, as we have pointed out, the Commission was dealing with a locked-in period. The revenues derived from the rates at issue had been impounded. The only question of substance in respect to that period was whether refunds should be made. The Commission decided that question, flatly and directly. No other question remained in those cases for decision. They presented no questions as to rates to be charged. Each presented the question whether a refund was due that customer for that past period and, if so, how much. Having made three determinations—(1) that there was a deficit of some $9,000,000 a year in revenues against cost of service, (2) that the increases involved totaled about five and a half million dollars and so, if allowed in full, would not wipe

[8] Modified to $54,525,315 after rehearing.

out the operating deficit, and (3) that any adjustments should be proportionate to all contract rates—it concluded that no refund was due on any contract, *i.e.*, in any 4(e) proceeding. Section 4(e) pertinently says that the Commission "may" order a refund of "the portion of such increased rates or charges by its decision found not justified." We cannot say that a deficit justifies or requires a refund or that the Commission was unlawfully arbitrary in reaching that result from the premises.

We think the Commission's course was reasonable and tenable. Surely, if only a single rate had been involved, and enough evidence were introduced to justify, under testing, a conclusion that the company was operating at a deficit under that rate, it would not be necessary that evidence be taken to establish the precise penny amount of the deficit in order to support a reasonable inference by the Commission that no refund was indicated. Of course, in the matter at bar a number of rates in separate cases were involved, but the principle of procedure and the scope of permissible inferences from basic facts are much the same as in the suggested illustration. We think the facts support the conclusion.

It is argued that the Commission did not declare the rates under consideration to be just and reasonable or the contrary; that, instead, it "terminated" the proceeding. The contention is that the Commission made no decision. We think the point is not well taken. The Commission did make a clear decision, after elaborate findings, upon the one substantive issue before it. It did say it "terminated" the proceedings, but it terminated them after deciding the basic and dispositive issue, and it entered an order on that decision. Its "termination" was much like that of a judge after he has rendered findings, conclusion and judgment.

Whether the Commission should have preceded its ultimate conclusion of no-refund with an intermediate conclusion of justness and reasonableness in the rates at issue, and whether it properly added the termination order to its decisive finding, seem to us to be immaterial queries.

The important feature is that the Commission reached and decided the critical substantial issue, rationally and upon detailed findings of basic facts upon an ample record.

This is not a *Minneapolis Gas*[9] situation, in which the Commission did nothing but simply terminated the proceeding without passing upon any of the disputed issues before it.

2. The case yields to clearer treatment if we next consider the part of the Commission's treatment which is last in chronological order, that is, the determination of rates for the future. As to these rates the Commission embarked upon the formulation of a new method of fixing just and reasonable rates for producers. It inaugurated hearings for that purpose. We think we need not explore the possibilities of success in that venture, or stop here to describe the projected scheme previously outlined in this opinion. In general it is referred to as an area-price method; it aims to establish proper prices for the gas rather than for the seller thereof. The Congress has confided the regulation of the natural gas industry to the Commission, not to the courts. The Supreme Court has said several times that the Commission is not bound to any one method or to known methods. The regulation of gas producers is a new project. Obviously, as is cogently pointed out in this record, it presents new and complex facts and problems. It would be foolish for the courts to hold that the Commission is bound to apply to these new conditions the methods and measurements designed and used for other and different regulatory purposes. We think it is clear that the Commission had ample authority to embark upon an effort to design suitable new standards for use in the regulation of producers when it found that the tools at hand were not suited to this purpose. The Commission abandoned the pending 5(a) proceeding in which it had been endeavoring to establish rates for the future by methods it now deems

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[9] *Minneapolis Gas Company* v. *Federal Power Commission*, U.S. App. D.C. , 291 F.2d 212 (D.C. Cir., 1961).

inadequate. We see no reason why it should not have done so.

3. The difficult part of the case before us concerns the second, or middle, part of the Commission's disposition. This involves the rates for the period from 1959 until the new system—or a new system—is designed and established. This period will be long, estimates running from four to fourteen years. The rates during this period may, theoretically, be (1) rates in effect without increases having been proposed after January 1, 1959, (2) rates proposed to be increased since that date and suspended under Section 4(e), (3) rates for which increases may be proposed after the present time, (4) initial rates, *i.e.*, rates under new contracts made after January 1, 1959.

To meet the need for interim regulation the Commission took several steps. It published the policy statement which we have described. That announcement contained several components. First, the Commission said that in determining its own *sua sponte* action in respect to rates (*i.e.*, suspending proposed increases or inaugurating inquiries into existing rates) it would be guided by the guide rates. Second, it said that persons attacking rates (*i.e.*, customers and consumers) would be required to present evidence as to the industry generally in the area concerned, as well as the traditional evidence relating to the individual producer involved. Third, it said that "[a]s experience and changing factors may indicate," it would change the areas designated and likewise change the guide prices. Fifth, it said it will use its guide rates in disposing of 4(e) (*i.e.*, suspended proposed increases) proceedings arising upon increases proposed since January 1, 1959.

Refraining from exploring the various arguments, and argumentative trails, pointed out to us by the parties, we come directly to the crux of this problem. Has the Commission power under the Natural Gas Act to do what it did? Can it adopt upon the basis of its own expertise and its files, without a record made in the open in respect to the

specific subject matter in issue, and without hearing, a set of guide lines by which it will be controlled in its regulatory functions during an interim period while it is attempting to perfect a suitable system for permanent regulation? We think it can.

In the first place, and throughout, we must remember that the Congress has power to direct the regulation of interstate commerce, and it has placed that regulatory power over natural gas in the Power Commission. We must remember that the problem at bar concerns a regulatory power. We are not considering adjudicatory, or quasi-judicial power. It has long since been established that rate-making is a legislative function, and it is so defined in the Administrative Procedure Act.

Regulation poses many difficult problems. New regulation poses acutely difficult problems. Solutions oftentimes develop slowly. Many illustrations of that fact could be called to mind.

What power has the Commission in respect to interim regulation while the permanent structure is being designed and erected? Must it use means and methods long established for use in respect to other and different regulatory necessities? Or may it design from its own judgment and accumulated data a new method designed for the new problem? The differences between a public utility, such as a pipeline rendering a service by means of a fixed plant and operation, and a producer, who discovers or buys a product where, when and under such terms as he may, and sells that product under contracts negotiated on the open market, are too evident to justify elaboration. Whether the method thus designed and put into use by the Commission is good or bad is no part of our problem. Our inquiry is whether it was within the orbit of statutory authority and whether it was within constitutional limitations. We turn to those questions.

The Natural Gas Act is broad in its bestowal of power. It declares that all rates demanded by a company in connection with the sale of gas in interstate commerce for resale

shall be just and reasonable. Section 4(a). A gas company files with the Commission schedules of its rates. Section 4(c). If a company proposes to increase a rate, it must file a new schedule. The Commission may then enter upon a hearing concerning the "lawfulness" of the proposed rate. Section 4(e). If the Commission, on its own motion or upon complaint, finds a rate unjust, unreasonable, unduly discriminatory or preferential, the Commission "shall" determine the just and reasonable rate. Section 5(a). Of course, constitutional restrictions apply; rates fixed by governmental authority cannot be confiscatory; all procedures must be by due process, that term conveying meanings differing according to the basic nature of the proceeding but always including that which is fair and decent according to the standards of our social order and time.

The statute contains no definition of a "just and reasonable" rate. It is established by tradition and by many court decisions that for a public utility, rendering service by use of fixed equipment, a just and reasonable rate is one which returns a fair profit upon the investment, or which supplies the utility with adequate revenues to command needed funds upon an economically reasonable basis. But what of a fair price for a commodity bought and sold by a merchandiser? Almost the whole of the economics of merchandising differs from the economics of public utility service. Are the just and reasonable prices of such a merchandiser limited to fair returns on his own investment and prices paid by him (and, if so, what investment and what prices), or are those prices reasonably measured by the fair prices for the product as measured by the open competitive market for the product, evaluated by Commission expertise and data on the whole of the market operation? Either criterion is a method of regulation. It seems to us that the choice must lie with the Commission.

Let us emphasize that we do not have before us at this time the question whether any rate set by the Commission as a guide rate falls within the area of reasonable compu-

tation. That question is emphatically left open by the Commission, and by us, for consideration when some one or more of the selected guide rates is attacked, by a producer, a customer, or a consumer. The problem here at this time is merely whether the Commission may embark upon this method of regulation. Since it is the Commission's judgment that this method is best suited for the regulation of these prices, for the determination of their justness and reasonableness, we find in the statute nothing to deny a trial of the method.

Of course, conceivably, justness and reasonableness from the standpoint of the consumer might be defined as limiting the vendor's return to a fair amount on his investment, and his price accordingly. But, if the government agency charged with the responsibility in the public interest finds, after elaborate accumulation of data, that such a measurement is unworkable, may not a fair price for the product reflected on the open market, after scrutiny and adjustment by the government agency concerning the factors which produced that price, be just and reasonable for the consumer? Of course the agency would be required to be alert for artificial impulses in such a fair area price, and the avenues of attack by consumers would have to be kept open without obstruction; but, if the latter is avowed, how could we assume in advance that the agency would not protect the consumer as it is charged by the Congress to do? The Commission is not here proposing to accept a field price, or any other price as is. It has announced guideline rates which it deems to be, on the basis of the internal data in its files on all the operators in the several areas, fair rates for the product in those areas. Such rates, thus determined, would seem to be just and reasonable rates for the consumers of the product. And, similarly, they would seem to be just and reasonable charges for the producers to make.

As to the constitutional question of confiscation, it would seem to us that the question should await the proof presented by a producer in respect to a particular rate in a particular area.

Thus we come to conclude that the interim method of regulation proposed by the Commission does not appear at this point in the process to be violative of either statutory or constitutional limitations.

It is urged upon us that the Commission has abandoned regulation of these rates for this interim period. We do not agree with that view. It has certainly changed the method of regulation, or, more precisely, the standards by which it will apply its regulatory power. It has abandoned case-by-case, contract-by-contract measurements on a cost-of-service rate-base basis. It has installed an area fair price measurement for the prices of the product to be sold. In so doing it has abandoned a method it finds to be unworkable and foolish in favor of a method it deems to be workable and just and reasonable. If that be so, instead of abandoning regulation it is making regulation effective. The choice it faced, at least in its own view, was not between regulation or no regulation but was between effective and ineffective regulation.

If, as some consumer interests fear, the new process turns out to be ineffective in the protection of their interests, the way is open for them to challenge the results; as we have pointed out, that way must be kept open. New rates and increases in rates proposed during this interim will be subject to suspension and refund, and so the rights of customers will be fully protected. The new method will also apply in 5(a) proceedings to any existing rate found to be unjust or unreasonable. Refunds cannot be ordered in the latter cases and so consumers bear the disputed rates during the period of the inquiry. But this same situation obtains in the present process of regulation; the application of the new criteria makes no change in this procedural aspect. In the case at bar the Commission has found, after elaborate consideration, that present rates result in deficits to the Company. Consumers have no tenable ground for complaint of such rates. So it seems to us that the interests of consumers are amply protected

during this interim period: at least a contrary effect should await the event for us to disturb the view of the Commission, based as it is upon this record.

There remains for discussion a point concerning two 4(e) proceedings which were not terminated. They involved proposed increases based upon escalator clauses in two of Phillips's contracts. These contracts were made before producers such as Phillips were subject to regulation. They were with pipeline companies, as customers, which were subject to regulation. The contracts provided that, if the pipeline companies were granted increases in the rates they could charge, Phillips in turn would receive increases in the rates it charged these customers. These customers had proposed increases, and they were pending in 4(e) proceedings. The Commission ordered that upon decisions in the customers' rate cases Phillips's cases would be acted upon.

Wisconsin and California contend that the Commission should now declare these escalator clauses to be illegal and void as against public policy. As a matter of fact the Commission has declared these clauses to be against the public interest and that they should be held inoperative. But, the Commission says, in so far as these cases of Phillips are concerned, action of the sort demanded by Wisconsin and California is premature. Action on these clauses, it says, should await action on the pending cases which in orderly processes present the problem for decision. We agree with the Commission.

Affirmed.

FAHY, *Circuit Judge, dissenting, with partial concurrence:* I am not able to agree that the order of the Commission terminating the section 4(e)[1] and section 5(a)[2] proceedings should be affirmed. I think the cases should be remanded to the Commission for decision.

While the Commission advances strong reasons for abandoning cost of service as a method of determining the justness and reasonableness of the rates of independent producers of gas, a careful reading of the Commission's opinion demonstrates that the Commission's conclusion that such a method is unworkable follows from a generalized view of the problem of producer rates rather than from the inability of the Commission to utilize the cost of service method in these Phillips cases.

Embarkation upon the area method preferred by the Commission does not necessitate judicial intervention, certainly not at this time; for judicial review must await a Commission order based upon that method. We should not seek to deter the Commission from pursuing such a method in future proceedings, or from using it in any proceedings already initiated along those lines. But it does not follow in my opinion that the Commission should be affirmed in failing to decide the present cases, though it may need to update the record. In the same breath as it were in which it describes the unworkability of the cost of service method the Commission itself accepts that precise method in finding that no refunds are to be required in the section 4(e) proceedings, stating:

> While we have found that the rate base method is not an effective means of regulating the producers' prices, evidence in this proceeding was presented almost entirely upon the cost basis and, of course, there were no ceiling prices issued by us at the time of the hearing. There was some field price evidence introduced, but if field prices could be employed in arriving at rates for Phillips, the evidence was incomplete and unrepresentative of Phillips' diverse sales. Therefore we shall proceed on

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[1] 52 STAT. 822 (1938), 15 U.S.C. § 717c (1958).

[2] 52 STAT. 823 (1938), 15 U.S.C. § 717d (1958).

> the basis of the evidence adduced in this case to reach conclusions, as reasonable, intelligent and logical as possible even though we know and have herein stated the difficulties inherent in determining a cost of service for Phillips using the rate method. This is clearly a lawful way to determine rates for Phillips as illustrated by the *City of Detroit* case,[11] and under the present record is the only possible method, and therefore we shall make every effort to reach a result by this means.
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> [11] *City of Detroit* v. *F.P.C.*, 230 F. 2d 810 (CADC), *certiorari* denied, 352 U.S. 829.

The Commission could as well have proceeded, with supplemental data, to decide the question of justness and reasonableness of the rates in the section 4(e) proceedings, and, also, to have determined under section 5(a) the just and reasonable rates to be thereafter observed and enforced.

This view is strongly fortified by the able decision of the Presiding Examiner. After an illuminating analysis of the voluminous record made on a cost of service basis he was able to propose definitive decisions. The record had been made with the cooperation of all parties, Phillips itself affirmatively acquiescing in the position that cost of service was the appropriate basis on which to proceed. Phillips' position, as the Examiner points out, was that its jurisdictional rates should be determined upon the basis of an overall cost of service.

It is one thing to say, as the Commission does, that the area method should hereafter be adopted, or even adopted in other cases which have not proceeded as far as those before us. It is quite another thing to say that the latter should not be decided under the standards of the Act because the area method was not used in preparing the record. Unless decided Phillips' challenged rates are left undetermined under the standards of the Acts since 1948, and apparently will continue to remain undetermined until some future day when new proceedings, now in an inchoate

status with no end in sight, are concluded. Difficult and complicated as the tasks of the Commission admittedly are I cannot agree after reading the Examiner's decision or the Commission's findings that the congressional mandate of section 4(e), which requires that these matters shall be decided "as speedily as possible," is being complied with, or that the responsibilities of the Commission under the Act are discharged in the situation resulting from the termination order.

These cases need not be treated as if they were ventures initiated in search of an ideal method of regulating the rates of independent gas producers. Having in mind the history of these proceedings, and the primary congressional purpose of consumer protection, it seems to me that decisions on the present record, supplemented as may be found to be reasonably necessary, would be far more likely to approximate fulfillment of the purposes of the Act than are the termination order and the resulting situation.

The Commission says it has a discretion to terminate as well as to initiate; but once it has exercised its discretion to initiate and has pursued the matter to the extent we find here its discretion to terminate is not as broad as was its discretion to initiate. The former becomes limited by the conditions existing at the time of its exercise. *Minneapolis Gas Co. v. Federal Power Comm'n.*——U.S. App. D.C.——, 294 F.2d 212. Compare *Eastern Air Lines, Inc. v. Civil Aeronautics Board.*——U.S. App. D.C.——, 294 F.2d 235.

The Commission has actually found Phillips' cost of service on the basis of the record made and has arrived on the same record at a proper rate of return, stating "this is clearly a lawful way to determine rates for Phillips as illustrated by the *City of Detroit* case, . . . and under the present record is the only possible method . . . ." In this manner the Commission has come so close to doing what it says it should not do as to demonstrate that it is able to do what it has failed to do.

The finding of the Commission in the section 4(e) proceedings that there could be no refunds because the cost

of service exceeded the revenues on the basis of the data for the 1954 test year, I think does not justify the order terminating all but two of the section 4(e) proceedings, or the Commission's invitation to Phillips to move to terminate all others which are still pending. The absence of a decision on the issue of justness and reasonableness of rates has the effect of leaving all rates subsequent to 1954 untested under the standards of the Act. Substance is not achieved merely by finding whether or not refunds were due on the basis of the 1954 data. A finding in that regard should not be independent of a finding of the just and reasonable rates. The former should follow from the fact that the just and reasonable rates are not exceeded by those in effect.

The decision of these cases under the standards of the Act not only would not preclude the Commission from embarking upon the area method, but it also would not preclude the Commission from correcting or modifying the decision should the area proceeding show such correction or modification to be desirable; nor do I think a decision on the present record, supplemented as may be needed, would preclude the Commission, pending conclusion of an area proceeding, from establishing guides, formulated however, with the aid of a decision in the present proceedings.

I agree with Judge Prettyman as to the prematurity of the request for action on two section 4(e) proceedings which have not been terminated.

APPENDIX B.

Judgment.

(Filed November 30, 1961.)

UNITED STATES COURT OF APPEALS,

FOR THE DISTRICT OF COLUMBIA CIRCUIT.

SEPTEMBER TERM, 1961.

No. 16,175.

STATE OF WISCONSIN AND PUBLIC SERVICE COMMISSION OF WISCONSIN,

Petitioners,

v.

FEDERAL POWER COMMISSION,

Respondent,

PHILLIPS PETROLEUM COMPANY,

Intervenor.

No. 16,177.

LONG ISLAND LIGHTING COMPANY, *et al.*,

Petitioners,

v.

FEDERAL POWER COMMISSION,

Respondent,

PHILLIPS PETROLEUM COMPANY,

PUBLIC SERVICE COMMISSION OF THE STATE OF NEW YORK,

Intervenors.

B-2

No. 16,180.

PEOPLE OF THE STATE OF CALIFORNIA AND PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA,

Petitioners,

v.

FEDERAL POWER COMMISSION,

Respondent,

PHILLIPS PETROLEUM COMPANY,

Intervenor.

On Petitions for Review of Order of the Federal Power Commission.

Before:

PRETTYMAN, FAHY and DANAHER,

Circuit Judges.

JUDGMENT.

These cases came on to be heard on the record from the Federal Power Commission, and were argued by counsel.

ON CONSIDERATION WHEREOF, It is ordered and adjudged by this court that the order of the Federal Power Commission on review in these cases is affirmed.

Per Circuit Judge PRETTYMAN.

Dated: November 30, 1961.

Separate dissenting opinion by Circuit Judge Fahy, with partial concurrence.

APPENDIX C.

Comparison of Average Unit Costs with Average Unit Revenues for All Major Producers whose FPC Rate Cases Have Progressed to Briefing or Decision.

Producer	Rate Case Cost Data: Docket	Test Year	Exhibit	Average Cost[6] (¢ per Mcf)	Average Revenue[6] (¢ per Mcf): 1954	1957	1960	Per Cent Increase 1957-60	1960 Revenue[5]: Total	Collected Subject to Refund	Collected Not Subject to Refund Amount (9)—(10)	Per Cent of Total (11) ÷ (9)
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)	(12)
Amerada Petroleum Corp.	G-18634	1957	61	13.4¢[1]	9.2¢	11.7¢	13.5¢	15.4%	$ 5,300,016	$ 418,786	$ 4,881,230	92.1%
Cities Service Co.	G-12780	[3]	[3]	[3]	[3]	[3]	17.7	[3]	8,972,261	1,053,599	7,918,662	88.3
Continental Oil Co.	G-16968	1955	FPC Staff Reply Brief	11.0	8.9	10.8	17.9	65.7	13,000,859	554,389	12,446,470	95.7
Gulf Oil Corp.	G-17813	1957	112	9.4¢*	9.6¢	11.5¢	15.4¢	33.9	29,028,130	4,727,179	24,300,951	83.7
Hunt Oil Co.	G-10414	1957	38	11.0	11.5	16.5	18.4	11.5	4,736,170	1,076,876	3,659,294	77.3
Ohio Oil Co.	RI60-92	1958	35	13.0¢	9.2	11.6	13.6	17.2	9,797,875	748,787	9,049,088	92.4
Phillips Petroleum Co.	G-1148	1954	Opinion 338	11.1	8.9	10.3	14.3	38.8	90,859,248	20,590,015	70,269,233	77.3
Shell Oil Co.	RI60-111	1959	44	19.3¢*	10.3	11.9	18.9	58.8	55,434,867	11,831,373	43,603,494	78.7
Sohio Petroleum Co.	G-18355	1958	51	15.2¢	9.0	9.7	19.0	95.9	4,749,664	2,581,297	2,168,367	45.7
Sun Oil Co.	G-18353	1957	67	12.3¢	8.6	12.0	16.0	33.3	17,524,295	1,981,586	15,542,709	88.7
Texaco, Inc.	G-8969	1956	104	8.5	10.8	15.3	17.8	16.3	31,835,212	2,885,156	28,950,056	90.9
Tidewater Oil Co.	G-13310	1957	FPC Staff Brief	10.7¢	10.0	14.1	18.2	29.1	17,903,668	2,936,339	14,967,329	83.6
Union Producing Co.	G-18354	1958	51	8.4¢	7.1	9.8	12.8	30.6	17,840,692	1,638,535	16,202,157	90.8

* Production taxes estimated.

[1] Using methods adopted by Respondent in Opinion No. 338 herein.

[3] Company not in existence in its present form in 1954 and 1957.

[4] Excludes Warren Petroleum Corp.

[5] Excludes revenues from sales made under other producers' rate schedules.

[6] Cost and revenue figures are not directly comparable, but are included to show approximate order of magnitude.

Source: (5) (6) and (7): Federal Power Commission, *Direct Sales by Producers of Natural Gas to Interstate Natural Gas Companies*, 1954, 1957 and 1960.

(9) and (10): F. P. C. Form 301 A for year ended 12/31/60.

APPENDIX D

Comparison of FPC Area Price Levels Set Forth in SGP61-1 with Highest Accepted Rate on File with FPC as of September 19, 1960, for Permanently Certificated Sale.

FPC Pricing Area	SGP61-1 Price Level for New Gas	Highest Permanently Certificated Rate as of Sept. 1960*	Comment or Explanation
Texas Dist. 1	15.0¢	14.7¢	
" " 2	18.0	18.0	
" " 3	18.0	20.0	See Note 1
" " 4	18.0	18.0	
" " 5	14.0	—	
" " 6	15.0	14.6	
" " 7B	14.0	10.5	See Note 2
" " 7C	16.0	16.0	
" " 8	16.0	16.0	See Note 3
" " 9	14.0	14.0	
" " 10	17.0	17.0	
So. Louisiana	21.5	22.0	See Note 4
No. Louisiana	17.0	18.5	See Notes 4, 5
Mississippi	21.5	21.5	
Okla.—Panhandle	17.0	17.0	
" Carter-Knox	16.8	16.8	
" Other	15.0	15.5	
Kansas	16.0	16.0	
N. M.—Permian	16.0	16.0	See Note 3
—San Juan	12.7	12.7	See Note 6
Colorado	14.6	16.0	See Note 7
Wyoming	15.0	15.0	

* Excludes rates authorized under temporary authority and rates for sales to commence more than three years in future.

Source: Adapted from F. P. C. Staff Exhibit No. 9 (*Ohio Oil Co.*, G-15385), as expanded and annotated from F. P. C. records.

NOTES

1. Prior to the announcement of the SGP levels in September 1960, the FPC had breached the 18¢ level in District 3 only twice—in *Peoples Gulf Coast*, G-19086, and in *Trunkline* G-15394. In both instances, certification came after the Public Service Commission of New York had been excluded. New York's exclusion from *Peoples Gulf* was subsequently reversed, 295 F. 2d 140 (D. C. Cir.

1961), thereby vacating the 20¢ certification in that case. Although New York's appeal from its *Trunkline* exclusion was dismissed as not timely filed, 284 F. 2d 200 (D. C. Cir. 1960), because of the circumstances surrounding New York's exclusion, the FPC does not regard the Trunkline levels as precedents. See brief of Federal Power Commission, filed February 12, 1962, in *Hunt et al* v. *F. P. C.*, 5th Cir. Nos. 19065 et al, pp. 11-18.

2. District 7B appears to be the only area where the SGP level (14.0¢) departs significantly from the prior high to 1960 (10.5¢). By way of possible explanation, we note the following: (1) by 1960, the 10.5¢ level was quite old, having been established many years previously; (2) very few new sales had been undertaken from District 7B in recent years; and (3) the SGP level for the two neighboring Districts, 7C and 8, is 16.0¢.

3. As of September 1960, the highest permanently certificated *wellhead* price for the Permian Basin of New Mexico and Texas District 8, which adjoins it, was 16.0¢ per Mcf. In August 1959, the FPC had authorized the sale of gasoline plant *residue gas* at 18.0¢ per Mcf, *Transwestern Pipeline Company*, 22 F. P. C. 391; the Transwestern opinion specifically notes that 16.0¢ was the highest wellhead price in the area.

4. The Louisiana prices are shown exclusive of tax reimbursement since this is the way in which they are shown by the FPC's Statement of General Policy. The Southern Louisiana price was modified slightly after the issuance of several Court of Appeals decisions reversing certifications at the level originally stated.

5. The only North Louisiana price in excess of 17.0¢—a single sale by Gulf Oil at 18.5¢—was apparently certificated in error; see Examiner's Decision in *Ohio Oil Company et al*, FPC Docket Nos. G-15385 et al, issued November 8, 1961, Mimeo., pp. 19-21.

6. In addition, the FPC had certificated a 15.9¢ sale in the San Juan Area for *gathered* gas; this price includes a gathering charge of at least 4.4¢. Southern Union Gathering Company Rate Schedule No. 1; see *Southern Union Producing Company*, G-7670, 14 F. P. C. 1220.

7. Includes 1¢ pressure adjustment. Moran Brothers, Inc., Rate Schedule No. 2.

APPENDIX E.

Natural Gas Act.

The pertinent provisions of the Natural Gas Act of June 21, 1938, c. 556, 52 Stat. 821; as amended, 15 U. S. C. §§ 717-717w, are as follows:

SECTION 4. (a) All rates and charges made, demanded, or received by any natural-gas company for or in connection with the transportation or sale of natural gas subject to the jurisdiction of the Commission, and all rules and regulations affecting or pertaining to such rates or charges, shall be just and reasonable, and any such rate or charge that is not just and reasonable is hereby declared to be unlawful.

* * * * * * *

(d) Unless the Commission otherwise orders, no change shall be made by any natural-gas company in any such rate, charge, classification, or service, or in any rule, regulation, or contract relating thereto, except after thirty days' notice to the Commission and to the public. Such notice shall be given by filing with the Commission and keeping open for public inspection new schedules stating plainly the change or changes to be made in the schedule or schedules then in force and the time when the change or changes will go into effect. The Commission, for good cause shown, may allow changes to take effect without requiring the thirty days' notice herein provided for by an order specifying the changes so to be made and the time when they shall take effect and in the manner in which they shall be filed and published.

(e) Whenever any such new schedule is filed the Commission shall have authority, either upon complaint of any State, municipality, or State commission, or upon its own initiative without complaint, at once, and if it so orders, without answer or formal pleading by the natural-

gas company, but upon reasonable notice, to enter upon a hearing concerning the lawfulness of such rate, charge, classification, or service; and, pending such hearing and the decision thereon, the Commission, upon filing with such schedules and delivering to the natural-gas company affected thereby a statement in writing of its reasons for such suspension, may suspend the operation of such schedule and defer the use of such rate, charge, classification, or service, but not for a longer period than five months beyond the time when it would otherwise go into effect: *Provided*, That the Commission shall not have authority to suspend the rate, charge, classification, or service for the sale of natural gas for resale for industrial use only; and after full hearings, either completed before or after the rate, charge, classification, or service goes into effect, the Commission may make such orders with reference thereto as would be proper in a proceeding initiated after it had become effective. If the proceeding has not been concluded and an order made at the expiration of the suspension period on motion of the natural-gas company making the filing, the proposed change of rate, charge, classification, or service shall go into effect. Where increased rates or charges are thus made effective, the Commission may, by order, require the natural-gas company to furnish a bond, to be approved by the Commission, to refund any amounts ordered by the Commission, to keep accurate accounts in detail of all amounts received by reason of such increase, specifying by whom and in whose behalf such amounts were paid, and, upon completion of the hearing and decision, to order such natural-gas company to refund, with interest, the portion of such increased rates or charges by its decision found not justified. At any hearing involving a rate or charge sought to be increased, the burden of proof to show that the increased rate or charge is just and reasonable shall be upon the natural-gas company, and the Commission shall give to the hearing and decision of such questions prefer-

ence over other questions pending before it and decide the same as speedily as possible.

[52 Stat. 822 (1938); 15 U. S. C. §717c]

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Section 5. (a) Whenever the Commission, after a hearing had upon its own motion or upon complaint of any State, municipality, State commission, or gas distributing company, shall find that any rate, charge, or classification demanded, observed, charged, or collected by any natural-gas company in connection with any transportation or sale of natural gas, subject to the jurisdiction of the Commission, or that any rule, regulation, practice, or contract affecting such rate, charge, or classification is unjust, unreasonable, unduly discriminatory, or preferential, the Commission shall determine the just and reasonable rate, charge, classification, rule, regulation, practice, or contract to be thereafter observed and in force, and shall fix the same by order: *Provided, however*, That the Commission shall have no power to order any increase in any rate contained in the currently effective schedule of such natural-gas company on file with the Commission, unless such increase is in accordance with a new schedule filed by such natural-gas company; but the Commission may order a decrease where existing rates are unjust, unduly discriminatory, preferential, otherwise unlawful, or are not the lowest reasonable rates.

[52 Stat. 823 (1938); 15 U. S. C. §717d]

* * * * * *

Section 19. (a) . . .

(b) Any party to a proceeding under this chapter aggrieved by an order issued by the Commission in such proceeding may obtain a review of such order in the court of appeals of the United States for any circuit wherein the natural-gas company to which the order relates is located or has its principal place of business, or in the United States Court of Appeals for the District of Columbia, by

filing in such court, within sixty days after the order of the Commission upon the application for rehearing, a written petition praying that the order of the Commission be modified or set aside in whole or in part. A copy of such petition shall forthwith be transmitted by the clerk of the court to any member of the Commission and thereupon the Commission shall file with the court the record upon which the order complained of was entered, as provided in section 2112 of Title 28. Upon the filing of such petition such court shall have jurisdiction, which upon the filing of the record with it shall be exclusive, to affirm, modify, or set aside such order in whole or in part. No objection to the order of the Commission shall be considered by the court unless such objection shall have been urged before the Commission in the application for rehearing unless there is reasonable ground for failure so to do. The finding of the Commission as to the facts, if supported by substantial evidence, shall be conclusive. If any party shall apply to the court for leave to adduce additional evidence, and shall show to the satisfaction of the court that such additional evidence is material and that there were reasonable grounds for failure to adduce such evidence in the proceedings before the Commission, the court may order such additional evidence to be taken before the Commission and to be adduced upon the hearing in such manner and upon such terms and conditions as to the court may seem proper. The Commission may modify its findings as to the facts by reason of the additional evidence so taken, and it shall file with the court such modified or new findings, which if supported by substantial evidence, shall be conclusive, and its recommendation, if any, for the modification or setting aside of the original order. The judgment and decree of the court, affirming, modifying, or setting aside, in whole or in part, any such order of the Commission, shall be final, subject to review by the Supreme Court of the United States upon certiorari or certification as provided in section 1254 of Title 28.

[52 Stat. 831 (1938), as amended, Aug. 28, 1958, Pub. L. 85-791, §19, 72 Stat. 947, 15 U.S.C. §717r.]